



State Investment Commission

Monthly Meeting Minutes

Wednesday, July 25, 2012

9:00 a.m.

Room 135, State House

The Monthly Meeting of the State Investment Commission (SIC) was called to order at 9:03 a.m., Wednesday, July 25, 2012 in Room 135, State House.

I. Roll Call of Members

The following members were present: Ms. Rosemary Booth Gallogly, Mr. Thomas Fay, Mr. Robert Giudici, Ms. Paula McNamara, Ms. Marcia Reback, General Treasurer Gina Raimondo and Executive Director of the Employees Retirement System of Rhode Island Mr. Frank Karpinski. Mr. Fay departed at 11:40 a.m.

Also in attendance: Mr. Thomas Lynch of Cliffwater, Alternative Investment Consultant to the Commission; Mr. John Burns of Pension Consulting Alliance (PCA), General Policy Consultant to the Commission; Ms. Lisa Tyrell, Mr. Mark Schafer, Mr. Steve Nazzaro, and Ms. Diane Johnson of State Street Corporation; Mr. Samir Pandiri, Mr. Bob Carroll, and Mr. Mark Sullivan of Bank of New York (BNY) Mellon; Mr. Christopher Nikolich, Ms. Patricia Roberts, and Mr. Greg Wilensky of Alliance Bernstein; Mr. Glenn Creamer and Mr. Matt Nelson of Providence Equity; Ms. Sally Dowling of Adler, Pollock & Sheehan, Legal Counsel to the Commission; Mr. Charlie Kelley, executive director of the Rhode Island Student Loan Authority; Mr. Kenneth Goodreau, chief investment officer and members of the Treasurer's staff and the Office of the Auditor General.

Treasurer Raimondo called the meeting to order at 9:03 a.m.

II. Approval of Minutes

On a motion by Ms. Reback and seconded by Mr. Fay, it was unanimously

VOTED: To approve the draft of the minutes of the June 27, 2012 meeting of the State Investment Commission.

III. Custodial Review / Presentations

Mr. Carroll of BNY Mellon introduced Mr. Pandiri, Mr. Sullivan, and himself. Mr. Pandiri said the firm has executed around 50-60 transitions in the last 3-4 years.

Ms. Booth Gallogly asked whether the firm owns the data during the transition and how well the firm knows the State's expectations and needs. Mr. Sullivan explained the firm has done transitions from State Street before and is familiar with the process.

BNY Mellon representatives left the room and the State Street team entered.

Ms. Johnson of State Street introduced Mr. Nazzaro, Mr. Schafer, Ms. Tyrell and herself.

Mr. Nazzaro described the core competencies of the firm.

Ms. Tyrell highlighted her experience with the Board and daily interaction with the Treasurer's staff. Ms. Tyrell acknowledged there have been some bumps along the way which have been dealt with.

Ms. Booth Gallogly asked how capital ratio matters in a custodial relationship. Mr. Nazzaro answered State Street will be able to continue investing in its business even when the economy is bad. The representatives of State Street thanked the Board for its time and exited the room.

General Treasurer Raimondo and Mr. Goodreau walked through the process which staff has been going through regarding custodian selection and explained a scorecard ranking BNY Mellon and State Street.

Ms. Booth Gallogly asked whether either firm's credit ratings would affect business. Mr. Goodreau responded there won't be an impact and stressed that those managing the State's cash would see the first warning signs.

Ms. Booth Gallogly asked about the services associated with pricing and Mr. Vincent Izzo explained these prices represented service at least at the level the State currently experienced.

Ms. Booth Gallogly asked about class action suit costs, and Mr. Izzo said things of that nature had been included.

Ms. Reback reminded the Board General Treasurer Raimondo had previously mentioned there were some unexpected findings in the process. General Treasurer Raimondo said staff thought both are high-quality providers, but through the process BNY Mellon had more competitive services with better pricing and staff pushed for BNY Mellon.

General Treasurer Raimondo added State Street's day-to-day accounting systems exhibited mistakes and there were delays in clarifying these and other issues. Ms. Booth Gallogly commented that these issues had not yet been raised to the board level. Mr. Giudici offered his input on what he thought was lackluster performance on behalf of State Street with respect to other clients.

Mr. Goodreau added cost savings would be well over \$250,000 each year and BNY Mellon is locking-in their price for up to 5 years.

Ms. McNamara wondered about impact of transition on staff, but Mr. Goodreau and Mr. Izzo reassured that the staff could handle it and even improve their processes.

Ms. Booth Gallogly was concerned about financial reporting and the general audit, and Mr. Izzo explained that BNY Mellon is very professional and aware of the State's situation.

Mr. Kem Edwards, Treasury staffer, added it is a good challenge to have a lot of great choices and in the end staff felt BNY Mellon was the best choice.

On a motion by Ms. Reback and seconded by Mr. Giudici, it was unanimously

VOTED: to hire Bank of New York Mellon as master custodian subject to successful negotiation and finalization of all documentation. Mr. Fay recused himself from the vote.

IV. Providence Equity Partners VII L.P. Presentation

Mr. Thomas Lynch said Cliffwater recommends a \$25 million investment in Providence Equity Partners VII, as part of the State's private equity investment program. He added Providence is Rhode Island's largest private equity relationship.

Mr. Creamer of Providence Equity introduced Mr. Nelson and himself. He mentioned Cliffwater's high level of due diligence on PEP VII. He highlighted Providence Equity has distributed \$8.3 billion this year, \$5.4 billion of that was gain. He also stated that in 78% of transactions, Providence is the only GP.

Mr. Creamer talked about PEP VII, which will be about \$5 billion, and will have 15-20 investments, with an average expected holding period of 4 years. The fund will keep some capital for follow-on investing. Information services will be a secondary focus. Europe is underweight, with an expected allocation of 10%. Transaction fees will be completely offset against management fees.

Mr. Creamer concluded by giving an overview of the market environment and the key to success was to be ready when markets were healthy.

General Treasurer Raimondo asked about the return on PEP V, and Mr. Creamer estimated the best case net IRR is 7%.

On a motion by Ms. Booth Gallogly and seconded by Mr. Fay, it was unanimously

VOTED: to commit \$25 million to Providence Equity Partners, for investment in PEP VII predicated on satisfactory completion of all due diligence. Ms. McNamara recused herself from the vote.

V. Fixed Income Presentation - PCA

Mr. Burns of Pension Consulting Alliance reiterated policy changes from the Board's meeting in June. He mentioned Core Fixed Income was 13.5% of the portfolio and PCA recommends splitting that between Pyramis and MacKay and terminating Brown Brothers core mandate and Taplin Canada. He stated fewer managers means higher allocation which means lower fees. All told, about \$475 million would be given to each of the recommended managers.

Mr. Goodreau stated the State will save roughly \$1 million in fees each year, with new fees estimated at a 13bp level, down from 22-24bp.

Mr. Fay asked if the fees mirror a high-quality index, and Mr. Goodreau responded affirmatively. Mr. Fay then asked whether the Barclays Aggregate Index was an appropriate benchmark and Mr. Goodreau and Mr. Burns responded affirmatively.

Ms. Booth Gallogly stressed the managers should know exactly what will be expected of them and General Treasurer Raimondo suggested mandates be drafted and presented to them for next meeting and the board agreed to vote next meeting.

VI. Global TIPS Presentation - PCA

Mr. John Burns of Pension Consulting Alliance reiterated policy changes from the Board's meeting in June. He mentioned as far as inflation-linked bonds, the State is only invested in those from the U.S. where yields are not attractive in this space, and expanding to a global portfolio would be beneficial. Mr. Burns recommended the State keep BBH as the inflation-linked bond manager and expand the firm's mandate to include foreign inflation-linked bonds. He mentioned the issue with hedging currency risk and said BBH was capable of doing this systematically.

Ms. Reback asked if BBH was the best, and Mr. Burns and Mr. Goodreau stated that the firm is more than capable and the best performance might carry the highest risk.

Mr. Burns also mentioned, while the mandate will be expanded, BBH will not increase fees. Similar questions were raised about the process of investing in something new without issuing an RFP, as in the Cored Fixed Income discussion. Mr. Goodreau said he was not comfortable holding a vote, given the conversation.

General Treasurer Raimondo suggested that the Board revisit this issue next month in full.

VII. 529 CollegeBoundfund Review

Ms. Roberts of AllianceBernstein introduced Mr. Nikolich, Mr. Wilensky and herself. Ms. Roberts said the CollegeBoundfund has about \$7.3 billion in it and Rhode Island has 25,000 accounts. Investors are attracted to age-based and stable value options, she added. Mr. Nikolich walked through the plan's performance and talked about specific funds.

General Treasurer Raimondo asked about changes to the plan that had been made last year. Ms. Roberts and Mr. Nikolich explained the additions of the Vanguard index funds, an international index fund and age-based fund options. Also, 3% of the State plan's assets were in the Vanguard funds, he said.

Mr. Wilensky talked about stable value options and the uncertain landscape of the market, considering wrapper providers had left the market. He explained AllianceBernstein was working with ING to figure out a plan with stable value wrappers moving forward. He stressed that with their economies of scale, an attractive 300bp beat over a money fund index was enjoyed by plan participants. He added from a cost perspective, plan participants will not be affected with the adoption of new wrapper contracts. He mentioned 13% of the State plan's assets are in the stable value option.

General Treasurer Raimondo remarked that Ms. Roberts and AllianceBernstein are always very responsive to the State's needs.

VIII. CIO Report

There was no CIO report.

IX. Legal Counsel Report

There was no legal update.

X. Adjournment

There being no other business to come before the Board, on a motion by Ms. Reback and seconded by Ms. Booth Gallogly the meeting adjourned at 11:57 a.m.

Respectfully submitted,



Gina M. Raimondo
General Treasurer